

Overview of 2 CFR Chapters I and II

The following information provides an overview of the proposed guidance, 2 CFR Chapters I and II. In the November 23, 2009, Executive Order 13520 on Reducing Improper Payments and the February 28, 2011, Presidential Memorandum on Administrative Flexibility, Lower Costs, and Better Results for State, Local, and Tribal Governments, the President directed the Office of Management and Budget (OMB) to work with Executive Branch agencies; state, local, and tribal governments; and other key stakeholders to evaluate potential reforms to federal grants policies.

The attached publication in the Federal Register requests that comments be received by OMB no later than 5 p.m. eastern standard time (e.s.t) on March 29, 2012. The publication provides three avenues in which comments may be submitted and a contact person for further questions on the process.

While these ideas are applicable to grants and cooperative agreements that involve state, local, and tribal governments as well as universities and nonprofit organizations, any current OMB circulars on cost principles covering all awards including contracts for these entities, reforms to cost principles will equally apply to all federal awards including contracts, except for contracts that are subject to “full coverage” under the Cost Accounting Standards (CAS) and subject to the relevant requirements under the Federal Acquisition Regulation (FAR).

I. Objectives and Background

A. Objectives

This reform effort includes reducing “red tape” that is attached to the more than \$600 billion the federal government in annual expenditures in the form of grants and cooperative agreements. The President instructed the OMB director to review and revise guidance concerning cost principles, burden minimizations, and audits for state, local, and tribal governments to eliminate, to the extent permitted by law, unnecessary, unduly burdensome, duplicative, or low-priority recordkeeping requirements and effectively tie such requirements to achievement of outcomes.

Not unlike the structure of the Federal Acquisition Regulations (FAR), OMB is considering implementing these reforms through the development and issuance of an integrated set of guidelines that are contained in one consolidated circular, while at the same time some provisions that vary among different types of recipients would be retained. The goal of such a streamlining increases the consistency, and decreases the complexity.

B. Background

For over a year the federal and nonfederal financial assistance communities have worked to carry out the President's direction that OMB and federal agencies form the interagency Council on Financial Assistance Reform (COFAR). It is a 10-member council which is composed of OMB's Office of Federal Financial Management (co-chair); and the eight largest grant-making agencies.

II. Reform Ideas for Comment

Public comment is being requested, so that OMB and federal agencies (and other stakeholders) can have the benefit of the public's input, views and perspectives at this stage, as we continue to evaluate these ideas for reform. The reform ideas under discussion include: a) reforms to audit requirements; b) reforms to cost principles and the cost principles for hospitals; and c) reforms to administrative requirements.

A. Reforms to Audit Requirements (Circulars A-133 and A-50)

This section discusses ideas for changing the audit guidance contained in Circular A-133 on Audits of States, Local Governments, and Non-Profit Organizations and in Circular A-50 on Audit Follow-up. There are five proposed changes:

1. Concentrating audit resolution and oversight resources on higher dollar, higher risk awards include: a) increasing the current threshold of \$500,000 to require a Single Audit to \$1 million. Those entities below the \$1 million threshold are not required to conduct Single Audits. This threshold increase proposes to reduce the administrative burden for audited entities and for auditing agencies, while allowing the agencies to concentrate their audit oversight and follow-up resources more closely on other entities that are higher dollar and higher risk; b) entities that expend between \$1 million and \$3 million in federal awards would undergo a more focused version of the Single Audit, which differs from current Single Audit requirements in that once a major program determination is made, auditors would review only two compliance requirements for those programs, which includes allowable and unallowable costs, and then agencies would have the discretion to select the second compliance requirement as they deem most appropriate; c) entities that expend more than \$3 million in federal awards would undergo a full Single Audit. These audits would be strengthened per the ideas in reforms 2-5 (below) to give agencies better tools to reduce improper payments and to eliminate waste, fraud, and abuse.

2. Streamlining the universal compliance requirements in the Circular A-133 Compliance Supplement. This reduces the types of compliance requirements tested and proposed to both reduce the audit burden on recipients and provide agencies with more risk-based audits. Agencies could add specific requirements under program specific tests and provisions where necessary.

3. Strengthening the guidance on audit follow-up for federal awarding agencies, could include; requiring agencies to designate a senior accountable agency official to oversee the audit resolution process; and, encouraging agencies to engage in cooperative audit resolution with recipients and to take a proactive approach to resolving weaknesses and deficiencies, whether they are identified with single, specific programs or cut across the systems of an audited recipient.

4. Reducing burden on pass-through entities and subrecipients by ensuring cross-agency coordination, which would involve making more explicit the existing requirement that federal awarding agencies are responsible for coordinating additional audits of a recipient entity with the federal oversight agency for audit for that entity, which reduces the number of subrecipients for which pass-through entities engage in duplicative follow-up efforts.

5. Reducing burdens on pass-through entities and subrecipients from audit follow-up. For those situations in which an entity receives a majority of its federal funds through direct grants from the federal government, and some federal funds through subawards, this would

require federal agencies to conduct audit follow-up of the subawards for those audit findings regarding financial or internal control systems that are not specific to the program delivery of the subawards.

B. Reforms to Cost Principles (Circulars A-21, A-87, and A-122, and the Cost Principles for Hospitals)

This section discusses ideas for: 1) consolidating the cost principles into a single document, with limited variations by type of entity; and 2) for indirect (“facilities and administrative”) costs, using flat rates instead of negotiated rates.

1. Reduce the administrative burden on all parties; and
2. Reduce the cost for indirect cost rate calculation and negotiation; the reduction in overall indirect costs. One option would be to establish a mandatory flat rate that is discounted from the recipient's already negotiated rate, or an option that would give recipients the option of accepting a flat rate or negotiating a rate. Recipients with a previously negotiated rate may have the additional option of accepting a discounted rate from their already negotiated rate. Discounted rates could be maintained for up to a 4-year period with minimal documentation, or raised through negotiation with full documentation. Entities with Cost Accounting Standards-covered contracts would still be required to use a negotiated rate for those contracts.
3. Exploring alternatives to time-and-effort reporting requirements for salaries and wages. This involves working with the federal grant and Inspector General (IG) communities to identify risks associated with justifications for salaries and wages and to identify possible alternative mechanisms for addressing those risks beyond current time-and-effort reporting requirements. Including the consideration and development of pilot programs that provide alternatives to time-and-effort reporting that may result in substantial reductions of the administrative burden currently associated with compliance, while enhancing compliance and stewardship.
4. Expanding application of the Utility Cost Adjustment (UCA) for research to more higher education institutions. This would expand application of the 1.3% indirect (facilities and administration) costs adjustment for utility costs of research to more institutions of higher education. Under this proposal, the UCA would be extended to those institutions that submit to their federal agency a utility cost study justifying an increase in utility cost reimbursement and an approved plan to reduce their utility costs over time. This opportunity to apply for the UCA to more institutions of higher education for research is aimed at resolving the equitable treatment by those academic institutions that have not been offered this opportunity since the UCA became available in 1998 to some institutions.
5. Charging directly allowable administrative support as a direct cost. This idea would involve clarifying the circumstances under which institutions of higher education and other entities where appropriate, may charge directly allowable administrative support as a direct cost. Included are project-specific activities such as managing substances/chemicals, data and image management, complex project management, and security.
6. Including the cost of certain computing devices as allowable direct cost supplies. This reform idea includes the cost of computing devices not otherwise subject to inventory controls (i.e. cost less than the organization's equipment threshold) as allowable direct cost supplies. These items would be a separate line-item in budget requests, but is not required as part of the inventory controls in place for equipment.

7. Clarifying the limit for an allowable maximum inventory of unused supplies, which would clarify that \$5,000 is an allowable maximum inventory of unused supplies. These supplies may be retained for use on another federal award, as long as the purchase was allowable at the time of the original agreement.

8. Eliminating requirements to conduct studies of cost reasonableness for large research facilities.

9. Eliminating restrictions on use of indirect costs recovered for depreciation or use allowances.

10. Eliminating requirements to conduct a lease-purchase analysis for interest costs and to provide notice before relocating federally sponsored activities from a debt-financed facility.

11. Eliminate requirements that printed "help-wanted" advertising comply with particular specifications, which updates the cost principles to reflect the media now used for those notices.

12. Allowing for the budgeting of contingency funds for certain awards.

13. Requesting that the Cost Accounting Standards Board (CASB) consider increasing the minimum limit for disclosure statements. This reform idea would involve OMB requesting that the (CASB) consider increasing the minimum limit for institutions of higher education to file a disclosure statement of cost-accounting standards from \$25 million to \$50 million in federal awards per year based on the average of the entity's most recent 3 years; and establish that the requirement no longer applies if an entity drops below the limit and is not required to file under current (CASB) requirements described at 48 CFR 9903.202-1; and remove exhibit A of Circular A-21 from future guidance.

14. Allowing for excess or idle capacity for certain facilities, in anticipation of increased usage, but only upon the grantee providing a multi-year plan for reaching full capacity of the data center.

15. Allowing costs for efforts to collect improper payment recoveries.

16. Specifying that gains and/or losses due to speculative financing arrangements are unallowable, that would update cost principles to address all types of debt arrangements.

17. Providing non-profit organizations an example of the Certificate of Indirect Costs, this is already provided for state, local, and tribal governments.

18. Providing non-profit organizations with an example of indirect cost proposal documentation requirements.

C. Reforms to Administrative Requirements

The following ideas for change would replace the government-wide common rule implementing Circular A-102 and revise Circular A-110, which include:

1. Creating a consolidated, uniform set of administrative requirements that would consolidate OMB Circulars A-102 & A-110 into a uniform set of administrative requirements for grant recipients, but still include limited exceptions by type of recipient.

2. Requiring pre-award consideration of each proposal's merit and each applicant's financial risk. Indicators of risk would include past financial, internal control, and programmatic performance. The outcome of the review should affect award decisions, and risk assessment may also affect terms and conditions. This change is aimed at ensuring greater transparency in the award making process, as well as higher quality of awarded projects, and at delivering improved results with less risk of waste, fraud, or abuse during implementation. In evaluating risks, agencies would consider financial stability; quality of management and internal control systems,

and the ability to meet the management standards prescribed in the amended guidance; history of performance; federal award Single Audit reports and findings for previous awards; and any other factors that may affect the applicant's ability to effectively all requirements imposed on recipients.

3. Requiring agencies to provide 90-day notice of funding opportunities. This reform idea requires federal agencies to provide 90-day advance forecast of funding opportunities in an updated Catalog of Federal Financial Assistance (CFFA) that will replace the existing Catalog of Federal Domestic Assistance (CFDA).

4. Providing a standard format for announcements of funding opportunities. Among other information, the opportunity announcement must include specific eligibility or qualification information and a clear description of all criteria used in agency review of applications for the grant opportunity. Further, agencies must disclose all terms and conditions that may be attached to the funded awards and general information regarding post-award reporting requirements, except for award specific terms and conditions determined during the pre-award process.

5. Reiterating that information collections are subject to OMB's Paperwork Reduction Act approval.

III. Questions for Comment

The attached Federal Register publication list the questions about the reform ideas that address issues which are of greatest interest to OMB at this stage of the process.